

Service Date: December 20, 1977

DEPARTMENT OF PUBLIC SERVICE REGULATION  
BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MONTANA

IN THE MATTER OF the APPLICATION	)	UTILITY DIVISION
by THE BUTTE WATER COMPANY for	)	
authority to increase rates and charges for	)	DOCKET NO. 6495
water service to its customers in the	)	ORDER NO. 4349A
ANACONDA, MONTANA service area and	)	
requesting ratification of the distribution of	)	
water service at no charge to certain	)	
customers.	)	

APPEARANCES

For the Applicant, Butte Water Company:

James A. Robischon, Esq., Poore, McKenzie, Roth, Robischon ~ Robinson, P.C., Attorneys at Law, Suite 400 Silver Bow Block, Butte. Montana

For the Protestant, Montana Consumer Counsel:

Geoffrey L. Brazier, Esq., Montana Consumer Counsel, 34 West Sixth Avenue. Helena, Montana

For the Commission:

Dennis R. Lopach, Esq., Staff Counsel  
Frank R. Buckley, Administrator, Utility Division

Before:

James R. Shea, Presiding Officer  
George Turman  
P. J. Gilfeather  
Thomas J. Schneider

FINDINGS OF FACT

A. General

1. The Butte Water Company, Applicant, is public utility furnishing water services to consumers in service areas in and around the cities of Butte and Anaconda and is subject to the regulatory jurisdiction of the Commission.

2. On the 18th day of February, 1977, Applicant filed an application in this Docket requesting authority from this Commission to increase its rates and charges for water service in the Anaconda, Montana, service area to produce annual revenues in the amount of \$69,734.
3. Pursuant to Notice of Public Hearing published on April 30, 1977, in the Montana Standard, a public hearing was conducted in the Deer Lodge County Courthouse, Anaconda, Montana, on May 26, 1977, at which time Applicant's witnesses appeared and were cross-examined on their testimony and exhibits. The Montana Consumer Counsel participated and presented testimony and exhibits concerning the matters and things covered by said application.
4. The evidence of record shows that the Applicant is entitled to a minimum annual revenue increase of \$43,996 from its customers in the Anaconda, Montana, service area which is not disputed by any parties to this proceeding.
5. By letter dated June 3, 1977, Geoffrey L. Brazier, Consumer Defender of the Montana Consumer Counsel, reaffirmed that he had no objection to a temporary rate increase of \$43,996 in this Docket. On the 7th day of June, 1977, Order No. 4349 in this Docket granted a temporary rate increase to the Applicant in the amount of \$43,996.

#### B. Revenues and Expenses

6. Operating revenues under present rates were estimated for the test year ended September 30, 1970, at \$140,232.00 with pro forma adjustments. The Commission finds that the adjustments made by the Applicant to its audited experienced revenue results are reasonable, and accepts the Applicant's test year revenues.
7. Operating and maintenance expenses were estimated for the test year at \$153,661.00 with pro forma adjustments. The adjustments made by the Applicant to its audited and actually experienced maintenance expenses are reasonable and are accepted.
8. No affirmative evidence was presented that challenged the Applicant's evidence relating to its claimed deductions for depreciation, taxes other than income, and other allowable operating revenue deductions, and the Commission finds that the total operating revenue deductions for the Applicant's test year, with pro forma adjustments under present rates are in the amount of

\$161,229.

9. Consumer Counsel Witness Wilson proposed revenue adjustments increasing Applicant's estimated revenues for recessionary conditions and slack water demand during the test period.

10. The Commission rejects Wilson's adjustments as they were not related to any known or measurable changes affecting the test period. All of the revenues of the Anaconda division come from the unmetered, flat rate customers. These revenues are unaffected by climatic conditions.

11. Consumer Counsel Witness Wilson proposed an offsetting expense adjustment for productivity increases.

12. The Commission rejects this adjustment also as it was not related to any known or measurable change affecting the test period. Witness Wilson on cross-examination admitted that his contentions were based on theory only and that the figures advanced were based upon studies unrelated to Applicant's operation that assumed that productivity increases will offset approximately one-half of wage and salary increases made during the period, (Tr 300, et seq.). This approach is strictly theoretical, and absent a convincing showing that the theory has any validity for Applicant's operation, will not be applied.

13. The interest cost relied upon by Applicant for its capital cost computation, as set forth in Applicant's Exhibit 26 (FRL) p. 33, is accepted by the Commission for all purposes, including the computation of test year income tax. Applicant utilized this figure only in computing interest expense on its hypothetical capital structure. The Commission agrees with Dr. Wilson, however, that consistency requires that this figure be used for all purposes (J. W. Wilson testimony, pp. 4-5).

14. The Applicant's method of computing its operating loss credits applicable to taxable income is accepted. However, these credits shall be amortized over a period of three years rather than the five year period advocated by Applicant. This amortization is consistent with Applicant's proposal to amortize rate case expense over a period of three years, and tends to assure that the credits will actually be used.

15. The Commission finds Applicant's test year federal income tax liability, following rate increase, to be \$921, which is computed as follows:

THE BUTTE WATER COMPANY  
ANACONDA DIVISION

12 Months Ended September 30, 1976

	<u>As 1/ Audited</u>	<u>Pro Forma 1/ Adjustments</u>	<u>1/ Adjusted</u>	<u>With Rate Increase</u>
1. Revenues	\$140,232		\$140,232	\$193,834 <u>2/</u>
2. Operation & Maintenance	138,241	\$ 15,420	153,661	153,661
3. Taxes (Other than income)	15,567	172	15,739	15,775 <u>1/</u>
4. Depreciation	5,849		5,849	5,849
5. Interest	29,422		29,422	11,741 <u>3/</u>
6. Miscellaneous Expenses	373		373	373
7. Net Before Taxes	(49,220)	(15,592)	(64,812)	6,435
8. Tax Adjustments	73		73	73
9. Taxable Income	(49,147)	(15,592)	(64,739)	6,508
10. Federal Income Taxes	(23,590)	( 7,484)	(31,074)	3,124
11. Unused Credits	2,197	7,484	16,681	
12. Credits Used				2,203 <u>4/</u>
13. Income Taxes Paid	(14,393)		(14,393)	921

1/ See applicant's Exhibit 21. p.8

2/ Rate Increase of \$53,602

3/ 8.48% of \$138,460

4/  $(159.00/3) (.48) (.0866) = 2,203$

### C. Rate Base

16. Applicant proposed a year-end original cost depreciated rate base of \$223,837 consisting of:

Utility Plant in Service	\$616,160
Less:	
Reserve for Depreciation	412,770
Add:	
Materials & Supplies	3,167
Cash Working Capital	<u>17,280</u>
	\$223,837

(C. M. Dunfee testimony p. 45, 1. 8 and Exhibit 21 (CMD), p.7).

17. Late-filed Exhibit S-1 (Revised) showed an average original cost depreciated rate base of \$202,406 consisting of:

Average Plant in Service	\$579,858
Less:	
Average Depreciation Reserve	397,899
Add:	
Materials & Supplies	3,167
Cash Working Capital	<u>17,280</u>
	\$202,406

18. Montana Consumer Counsel Witness Wilson accepted the Applicant's rate base, with the exception of a negative adjustment to the cash working capital which he advocated in his rebuttal testimony.

19. The Commission rejects the negative adjustment to cash working capital as it finds Applicant's policy of promptly paying its bills to be a desirable one. Firms doing business with the Applicant should not be expected to supply the working capital for the payment of the Applicant's bills.

20. The Commission finds that an average rate base is appropriate in this proceeding. A rate base which reflects average investment in plant in service achieves a more proper matching of operating income with the investment that produced that income during a given test year period. Proper rate making requires that the test year revenues and expenses realistically reflect expected performance under the test year rate base.

### D. Rate of Return

21. Butte Water Company has an actual capital structure of:

	Amount	% of <u>Capitalized</u>
Demand Notes to Parent	\$ 400,000	16.9
Accounts Payable to Parent	473,176	19.9
Common Equity	<u>1,499,231</u>	<u>63.2</u>
Total	\$2.372,407	100.

(Exhibit 14 (CXS), p. 3 and Exhibit 26A (FRL), p. 80).

22. The Commission agrees with Applicant that for the cost-of-capital determination, it is appropriate to use a hypothetical capital structure of 65% debt and 35% equity (Exhibit 26A (FRL) p. 80). This capital structure approximates the type of structure commonly employed in the utility industry.

23. The overall cost of debt in the hypothetical capital structure is 7.6 percent (Direct testimony, (FRL), p. 81).

24. The Butte Water Company is a third-tier subsidiary in a vertically pyramided corporate structure, with Butte Water being wholly owned by Anaconda and Anaconda in turn wholly owned by A.R.C.O., (J. W. Wilson testimony, p. 6, 1. 35-48).

25. A reasonable return on common equity to the ultimate equity investors of Butte water is 13 percent (J. W. Wilson testimony, p. 7, 1. 23)

26. An 8.525% rate of return allowance for Applicant will yield a 13% return to the ultimate equity investors (J. W. Wilson testimony, p. 7, 1. 19-23 and Exhibit JW 10).

#### E. Revenue Requirement

27. In order to produce a return of 8.525% on the Applicant's average original cost depreciated rate base, the Applicant will require additional annual revenues in the amount of \$53,602 from its Anaconda, Montana, water utility. Of this total amount the Commission has heretofore authorized additional revenues in the amount of \$43,996.00 in our Order No. 4349.

28. Applicant is, therefore, entitled to additional revenues additional to those granted by the

Commission in Order No. 4349 in this Docket in the amount of \$9,606.

29. Applicant's test year pro forma operating revenues, expenses and rate of return are summarized as follows:



THE BUTTE WATER COMPANY  
ANACONDA DIVISION

12 Months Ended September 30, 1977

	As <u>1/</u> <u>Audited</u>	Pro Forma <u>1/</u> <u>Adjustments</u>	Pro Forma Present Rates <u>1/</u> <u>Adjusted</u>	With Rate <u>Increase</u>
1. Revenues	\$140,232		\$140,232	\$193,834 <u>2/</u>
2. Operation & Maintenance	138,241	\$ 15,420	153,661	153,661
3. Depreciation	5,849		5,849	5,849
4. Taxes (Other than income)	15,567	172	15,739	15,775 <u>1/</u>
5. Income Taxes	(14,393)		(14,393)	921 <u>3/</u>
6. Miscellaneous Expenses	373		373	373
7. Total Deductions			161,229	
8. Net Operating Revenues	(5,405)	(15,592)	(20,997)	17,255
9. Rate Base	223,837	4,427	228,264	202,406 <u>4/</u>
10. Rate of Return	(2.41%)		(9.43%)	8.525% <u>5/</u>

1/ See applicant's Exhibit 21. p.10

2/ Rate Increase of \$53,602 (Finding No. 28)

3/ Finding No. 15

4/ Finding No. 17

5/ Finding No. 26

## F. Other Matters

30. The allocation of the Applicant's revenue requirements among its various customer classes was tested against a cost or service study conducted for the Applicant by its consultants. The allocation proposed by the Applicant is reasonable under the circumstances and the Commission will accept a tariff of rates and charges based upon the Applicant's proposed rate spread.

31. Applicant's proposed rate structure perpetuates an antiquated rate design which is of highly dubious merit. Unfortunately, the record lacks sufficient evidence to afford a basis for any other rate design. Applicant shall present as a part of its next general rate increase application a substantially simplified and rational rate design.

32. The Commission finds that the long-standing practice of the Applicant in supplying water service at no charge to the classes of customers shown on Exhibit No. 13 (CWY) is a reasonable and non-discriminatory practice, and that it may be continued in the discretion of the Applicant.

## CONCLUSIONS OF LAW

1. This Commission has jurisdiction over the Applicant and the level of rates and charges which it may charge under R.C.M. 1947, Section 70-101, et seq.

2. The Applicant is entitled to additional revenue to that revenue ordered by this Commission as a temporary rate increase in Order No. 4349 in this Docket.

3. The rate of return resulting from a \$53,602 annual revenue increase will not exceed a fair return on Applicant's properties devoted to the service of its Anaconda, Montana customers. The resulting return will comply with the constitutional requirements established in the case of *F.P.C. v. Hope Natural Gas Co.*, 320 U.S. 591 (1944)

4. The allocation of Applicant's revenue requirements among its various customer classes,

as proposed by Applicant, is fair, reasonable and non-discriminatory and will be accepted by the Commission for this proceeding.

5. The average rate base employed in this proceeding is a proper means of measuring Applicant's properties at risk during the test period, and produces a better matching of test year investment, revenues and expenses than coca a year-end figure.

6. The Applicant, in its discretion, may continue the long standing practice of supplying water service at no charge to the classes of customers identified in Finding of Fact No. 32.

### ORDER

IT IS ORDERED that the Applicant shall submit for Commission approval a schedule of rates and charges which will produce a total annual revenue additional to that now being collected of \$9,606 for services rendered on and after January 1, 1978.

DONE IN OPEN SESSION this 20th day of December, 1977, by a vote of 3 to 1.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION.

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GORDON E. BOLLINGER, Chairman

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THOMAS J. SCHNEIDER, Commissioner

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JAMES R. SHEA, Commissioner  
( Voting to dissent)

ATTEST:

Gail E. Behan  
Secretary

(SEAL)